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Decision 03-02-032 February 13, 2003

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Southern California Edison Company (E333-E) for Authority to Institute a Rate Stabilization Plan with a Rate Increase and End of Rate Freeze Tariffs.	Application 00-11-038 (Filed November 16, 2000)
Emergency Application of Pacific Gas and Electric Company to Adopt a Rage Stabilization Plan. (U 39 E)	Application 00-11-056 (Filed November 22, 2000)
Petition of THE UTILITY REFORM NETWORK for Modification of Resolution E-3527.	Application 00-10-028 (Filed October 17, 2000)

OPINION ON MUNICIPAL FEES RELATING TO ELECTRICITY SALES BY CALIFORNIA DEPARTMENT OF WATER RESOURCES

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OPINION ON MUNICIPAL FEES RELATING TO ELECTRICITY SALES BY CALIFORNIA DEPARTMENT OF WATER RESOURCES

I. Background

This decision resolves issues regarding the collection and remittance of franchise fees in connection with electric power sales of the California Department of Water Resources (DWR) pursuant to Assembly Bill (AB) 1 of the First Extraordinary Session (Stats. 2001, Ch. 4), hereafter referred to as AB1X. We address this issue pursuant to Decision (D.) 02-02-052, in which we allocated the DWR revenue requirement among customers in the service territories of the major electric investor-owned utilities (IOUs): Pacific Gas & Electric Company (PG&E), Southern California Edison Company (SCE), and San Diego Gas & Electric Company (SDG&E).

As prescribed under Public Utilities Code Sections 6000- 6302, municipalities grant franchises to IOUs to use public rights-of-way to construct and maintain the physical facilities necessary for the IOUs to provide gas and electric service to customers. The IOUs are authorized to locate facilities on public property in exchange for the payment of a franchise fee. During the course of the DWR revenue requirement proceeding, however, a dispute arose involving the question of whether, or on what basis, franchise fees may be assessed, collected, and remitted to municipalities for electric power sales made by DWR to customers pursuant to AB1X.

Issues in dispute include what are the legal rights of municipalities to be paid franchise fees on DWR power sales, and what are the legal obligations of DWR to collect and/or remit franchise fees associated with its power sales. There are also unresolved questions as to the IOUs' obligations to remit franchise fees to municipalities on DWR power sales, and the extent to which current IOU

retail rates already include (or should include) a provision for such franchise fees. In D.02-02-052, we did not reach a final resolution of these questions, but directed the assigned Administrative Law Judge (ALJ) to take further comments on the pertinent legal and factual issues as a basis for further Commission action.

In accordance with the directive in D.02-02-052, an ALJ's ruling was issued on April 3, 2002, soliciting comments on the above-referenced issues. Comments were filed by PG&E, SDG&E, and SCE. Various parties representing local government interests also filed comments. These included the City of San Diego and the City and County of San Francisco (CCSF). CCSF is joined in its comments by the following cities: Berkeley, Davis, San Leandro, and Sunnyvale. The County of Los Angeles filed separate comments. The mayors and municipal administrators of various cities, although not parties to the proceeding, sent letters to the ALJ in support of the comments of the parties representing municipal interests.[1] DWR is not a formal party to the proceeding, but submitted a memorandum to the Commission, served on parties, expressing its views on the subject. The filed comments form the record for the conclusions we reach in this order.

II. Municipalities' Rights to Franchise Fees and Municipal Surcharges

A. Positions of Parties

DWR asserts that it is not responsible for the collection or remittance to municipalities of franchise fees relating to electric power sales that it makes under AB1X. DWR did not include any provision for franchise fees in its revenue requirement implemented in D.02-02-052. Although DWR-provided power flows

[1] These letters shall be placed in the correspondence file for this proceeding.

over IOU facilities that are subject to the franchise authority of municipalities, DWR, itself, does not own physical facilities in public rights-of-way. DWR has no franchise agreement with any municipality nor does it operate a franchise.[2] The emergency legislation establishing the DWR's responsibilities for buying and selling power identifies the categories of charges the DWR is to collect, but does not include municipal surcharges or franchise fees.[3] Since the state legislature has carefully delimited the fees and expenses that the DWR may collect, DWR argues that municipal charters may not expand the DWR's statutory role to include remittance of franchise fees.

DWR recommends that the IOUs continue to collect surcharges and remit franchise fees to municipalities on revenues from sales of DWR power in accordance with the IOUs' franchise fee agreements, subject to an appropriate cost recovery mechanism for these payments.

The IOUs argue that they have no legal obligation to remit franchise fees on DWR-supplied power. Under the provisions of Public Utilities Code Section 6006, franchise fees are calculated based upon the "gross annual receipts of the grantee arising from the use, operation, or possession of the franchise." Since the "grantee" of the franchise is the IOU, they argue, only the "gross annual receipts" from IOU sales are subject to franchise fees. The IOUs exclude those revenues that are not sources of IOU earnings for franchise fee purposes. Such excluded revenues include interdepartmental sales and collections from others, *e.g.*, users taxes.

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[2] *See e.g., Saathoff v. City of San Diego* (1995) 35 Cal. App. 4th 697

[3] *See*, California Water Code Sections 80106, 80110.

The IOUs argue that they are not obligated to remit franchise fees for DWR-provided power under the terms of their franchise agreements, because the DWR-provided power is not the property of the IOU. Under Water Code Section 80110, DWR retains title to power that it sells to end users. The IOUs thus view the "gross revenues" from DWR sales as belonging to DWR, whereas franchise fees referenced in Public Utilities Code Sections 6000 through 6302 apply solely to the revenues belonging to the IOU. Thus, they argue, revenue from the sale of power by DWR is not "receipts of the grantee" that the IOUs include for computing franchise fees pursuant to Section 6006.

While contending they are not responsible for franchise fees on DWR revenues under Sections 6000-6302, SDG&E and SCE do believe that local governments are entitled to "municipal surcharges" on DWR revenues as prescribed by Public Utilities Code Sections 6352 through 6354.1. These sections codify provisions of the Municipal Lands Surcharge Act ("the Act") which was created in 1993 by Senate Bill (SB) 278 which imposed a surcharge on gas and electric sales by entities other than the incumbent utility.[4]

The statutory provisions authorizing municipal surcharges were enacted in response to changes in California gas and electricity industries as they began to be partially deregulated, permitting entities other than the IOUs to sell to retail customers. Because then-existing statutory requirements for remittance of franchise fees only applied to revenue from sales of electricity by IOUs, non-utility commodity sales would result in reduced IOU revenues and,

[4] SB 278 requires the surcharge to be applied to gas and electricity sales, but did not provide for the computation of the surcharge on electricity sales. That requirement was added by SB 703 (1997).

consequently, reduced franchise fees paid by IOUs to municipalities. The Legislature recognized that reducing franchise revenues simply because the commodity was supplied by an entity other than the franchised IOU would be unfair both to municipalities and customers.

SDG&E and SCE believe that, consistent with the intent of SB 278, customers obtaining power from DWR have a separate obligation under Section 6352 through 6354.1 of the Code to pay such "municipal surcharges" to local governments. Likewise, SDG&E and SCE believe that the IOUs have an obligation to bill, collect, and remit such municipal surcharges. SDG&E believes that end-use customers receiving DWR energy are responsible for municipal surcharge payments.

PG&E disagrees with SCE and SDG&E on this point. PG&E argues that under current law, neither utility franchise fees nor municipal surcharge fees are payable to cities and counties on the power delivered by DWR. PG&E does not believe that current franchise fee and municipal surcharge statutes adequately address how cities and counties should be compensated related to DWR power sales. Under the statutory scheme, "energy transporters" are responsible for collecting the surcharges and remitting fees. PG&E argues that under the Act, DWR serves the role of such an energy transporter in similar fashion to electric service providers (ESPs).[5] Yet, the statute defines a "transportation customer" as an entity *other than* "the State of California or a political subdivision thereof." Therefore, PG&E believes the unintended consequence of AB1X is to exempt DWR, as an agency of the State of California, from the municipal surcharge.

[5] *See*, Water Code § 80106.

DWR claims that it is not an "energy transporter" as defined by Public Utilities Code Section 6351, and thus is not required or authorized to collect surcharges or remit franchise fees to municipalities under that statutory provision. DWR argues that Public Utilities Code Sections 6353 and 6354 require the energy transporter (*i.e.,* the IOU) and not the seller (*i.e.,* DWR) to calculate, collect, and remit municipal surcharges. DWR does not consider itself responsible for collecting municipal surcharges pursuant to the California Public Utilities Code Section 6350 *et seq.*

Parties representing municipalities argue that they are entitled to compensation on DWR power sales, and that the Commission should order DWR or the IOUs to remit appropriate fees. The Cities generally contend that both the IOUs and DWR are jointly liable for the payment of franchise fees on DWR power sales. The Cities argue that under an "implied covenant of good faith and fair dealing," the IOUs must honor their obligations to the municipalities, including the payment of franchise fees. Because DWR stands in the shoes of the IOUs for purposes of purchasing power, the cities claim, the IOUs should be obligated to collect franchise fees on this power and provide such fees in full to the municipalities. The municipalities claim the Commission has sufficient discretion to require remittance of franchise fees on power supplied by DWR for utility customers without additional legislation or "clarification."

City of San Diego argues that under city charters, franchise fee obligations are not confined to revenue from transmission and distribution, but also include revenue from generation sold to users. The City argues that the franchise fee obligation applies irrespective of whether the generation is supplied by the IOU, a third party, or DWR. The San Diego City Charter Section 103.1

states that no person may "establish and carry on any business within the said City which is designed to or does furnish services of a public utility nature" to the inhabitants of the City without consent of the City manifested by ordinance. The City argues that selling power is such a business even if DWR does not own the lines. Section 105 of the San Diego City Charter requires payment of franchise fees by persons furnishing such service.

Since both SDG&E and DWR are jointly involved in DWR's electric energy sales in the City, and because DWR could not sell its power without the participation of the utility, City of San Diego argues that they are jointly and severally liable for franchise fees on all revenue derived from the entirety of those sales. City of San Diego claims that while DWR is not obligated to charge franchise fees to its customers as a line item, it is legally obligated to pay a percentage of its gross revenue to the City as a franchise fee.

City of San Diego claims that the municipal surcharge was not intended to apply to DWR, but was designed instead solely for the direct access market to address the fact that unbundling would inadvertently put multiple service providers in a position of doing business with the cities, resulting in disparity in franchise fee burdens for customers and uncertainty for the cities. (*See* Stats.1993 ch 233 Section 1, effective July 30, 1993). City of San Diego claims the municipal surcharge was the legislature's expedient approach to addressing an inadvertently created problem, but does not recognize the constitutional basis of the charter cities' rights to franchise fees, and it does not replace those rights. Thus, the City claims it is not legally obliged to permanently accept municipal surcharges as a substitute for franchise fees.

Both the City of San Diego and CCSF claim that municipal surcharges only partially protect the cities' financial interest, and that franchise fee

remittances on DWR sales should therefore be required. Otherwise, they believe the status quo should continue until a more permanent solution is adopted to avoid serious harm to the municipalities and claims of rate discrimination. The County of Los Angeles, however, expresses no objection to receiving municipal surcharges (in lieu of franchise fees) on DWR sales. Likewise, several mayors and city administrators throughout California (although they are not parties to this proceeding) sent letters to the ALJ in favor of municipal surcharges as an acceptable form of compensation for DWR power sales.

B. Discussion

The question before us is whether the rights of the municipalities to be compensated for the sale of electric power utilizing IOU facilities that are subject to a franchise agreement apply to sales by DWR made pursuant to AB1X.

1. Obligations to Pay "Franchise Fees"

Under the provisions of Code Section 6006, the relevant determinant of franchise fee liability depends upon whether the funds in question constitute "receipts" belonging to the IOU (*i.e.*, the "grantee" of the franchise). Under the legal provisions of Water Code Section 80110, DWR retains legal title to all power sold by it to end use customers. Although the IOU acts as collection agent for DWR, the IOU never takes title to the power, and accordingly, is merely a temporary custodian of the receipts from the sale of DWR power.[6] Thus, DWR revenues do not constitute "receipts" belonging to the IOU for purposes of

[6] Water Code Section 80104 further states that: "[u]pon the delivery of power to them, the retail end use customers shall be deemed to have purchased that power from the Department. Payment for any sale shall be a direct obligation of the retail end user to the Department."

computing franchise fees. If we were to treat DWR receipts as property of the IOU, we would be in violation of Water Code Section 80110.

Moreover, there is nothing in the Water Code that identifies either franchise fees or municipal surcharges as elements of the revenue requirement that DWR collects. Likewise, because DWR has responsibility to make the determination that its revenue requirement is "just and reasonable" under Public Utilities Code Section 451, we cannot compel DWR to collect such fees on its power sales, or to remit fees to municipalities.

DWR is not legally liable for remittance of franchise fees under those provisions of the Code that apply only to franchisees. DWR does not own facilities subject to a franchise or hold a franchise agreement with any municipality. The terms of DWR power sales are not defined by municipal charter, but by statewide emergency legislation. DWR procurement under AB1X is not subject to municipal charter authority.[7] The emergency legislation under AB1X creating the DWR's power purchase responsibilities stated that the problems addressed by the legislation had a statewide impact. Although cities may legislate upon matters of statewide concern, in the event of conflict with state law, state law controls.[8] Moreover, the courts have instructed that any doubt about whether a matter is a municipal affair or has broader state concern must be resolved in favor of the legislative authority of the state.[9]

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[7] *See*, California Water Code § 80000(a).

[8] *See, e.g., Pipoly v. Benson* (1942) 20 Cal.2d 366, 369-370, 125 P.2d 482.

[9] *See, e.g., Abbott v. City of Los Angeles* (1960) 53 Cal.2d 674, 681, 3 Cal.Rptr. 158, 349 P.2d 974; *Younger v. Berkeley City Council* (1975) 45 Cal.App.3d 825, 830, 119 Cal.Rptr. 830.

The mere fact that the DWR sales are delivered utilizing facilities of the IOU that are subject to a franchise agreement does not, of itself, make DWR subject to remittance of franchise fees. Otherwise, if nonutility third-party sales were subject to franchise fees merely by virtue of being delivered over franchised facilities, there would have been no need for the California Legislature to enact statutory provisions establishing municipal surcharges for such sales pursuant to Code Sections 6360-6354.1. Yet, the Legislature expressly recognized that because third party sellers of electricity do not have franchise agreements with municipalities, their sales are not subject to franchise fees, and thus, an alternative funding source was needed to protect against loss of revenues by municipalities.

Accordingly, we conclude that the requirements for remittance of franchise fees under Code Sections 6000-6302 apply only to the revenues on sales made by the franchisee (*i.e.*, the IOU) within the limits of the municipality for which the franchise is awarded. Because the power sold by DWR is not the property of the IOU, the revenues on the sale of DWR power likewise is not the property of the IOU franchisee. Thus, the IOU is not liable for remittance of a franchise fee on DWR sales pursuant to Code Sections 6000-6302.

2. Obligations to Pay "Municipal Surcharges"

We conclude, however, that the key to resolving the municipalities' concerns regarding compensation for DWR sales lies in the provisions of Public Utilities Code Sections 6350 through 6354.1. Although DWR power purchases under AB1X were not specifically contemplated at the time the municipal surcharge was enacted, the statute nonetheless required customers purchasing power from a third party to be liable for the municipal surcharge. We recognize that DWR's entry into the electric market under AB1X was intended to backstop

the IOUs rather than to compete against them. Nonetheless, the end result still entailed the sale of electric power to end use customers by an entity other than the IOU. The stated legislative intent behind enactment of the municipal surcharge was to protect the financial integrity of local government as a portion of the traditional IOU revenue base for gas and electric service was opened up to the competitive market. Thus, whether the loss of IOU revenue was due to competition or due to DWR backstopping the IOU, the underlying legislative intent still is the same. Therefore, we conclude that DWR sales are a special category of third-party electricity sales that are subject to municipal surcharges under the provisions of Code Sections 6351 through 6354.1 which codified the Municipal Public Lands Use Surcharge Act.

The legislative intent of the Act was to keep municipalities financially whole in the changing regulatory environment of the 1990's, recognizing that customers receiving power over IOU facilities should not escape their obligation to pay franchise fees because the power was purchased by a non-utility seller. Those customers would have paid franchise fees on such power had it been purchased from the IOU. It would be inconsistent with the intent behind the municipal surcharge act to deprive municipalities of compensation for DWR sales merely by virtue of the fact that the IOUs rely upon DWR to provide a portion of the power that they previously supplied to their own customers.

Under the Act, the municipal surcharge is assessed on "transportation customers," and provided to cities and counties. In this regard, Section 6352 (a) states that "[n]otwithstanding any other provision of law, a transportation customer who receives transportation service on [an] electric transmission or distribution system . . . subject to a franchise agreement executed pursuant to this

division from an energy transporter shall be subject to a surcharge as defined in Section 6353."

A "transportation customer" is defined under Section 6351(c) to include every person (other than certain state entities) purchasing electricity from a third party and transporting such electricity on an energy transporter's transmission or distribution system. The exclusion of political subdivisions of the state of California from the definition of "transportation customer" raises the question of whether DWR is a "transportation customer" and whether its sales are thereby exempt from the municipal surcharge. Although DWR is a political subdivision of the state of California, we conclude that DWR power sales revenues nonetheless give rise to surcharge revenues under the Act because it is the end use customer, not DWR who is considered as the "transportation customer" under Section 6351.

DWR is more properly designated as a third-party supplier (referred to in Section 6351(c)) from whom the retail customer purchases electricity. The IOU serves the role of "energy transporter," as defined under Section 6351(b), since its facilities are used to deliver DWR power. We conclude therefore that end use customers of DWR are "transportation customers" and are responsible for municipal surcharges on DWR power sales in that capacity. There is no reason to treat sales by DWR differently than sales through other third-party suppliers, where the IOU acts as a collection agent, collecting from transportation customers and paying the municipality a surcharge based on such third-party sales pursuant to Section 6350 *et seq.* The IOUs already have in place a process for collecting and remitting municipal surcharges relating to third-party revenues. It is appropriate, therefore, for the IOUs to bear responsibility for

collecting and remitting municipal surcharges owed to the municipalities by customers of DWR, as well.

Parties representing municipalities provide no citation to support the claim that municipal surcharges only "partially" protect cities' financial interest in comparison to franchise fees. Section 6350 expressly states that the intent of the municipal surcharge is "to replace, but not increase, franchise fees that would have been collected pursuant to this division if not for changes in the regulatory environment such as the 'unbundling' of the gas industry." Moreover, as prescribed in Section 6353(d), the municipal surcharge is calculated by applying the franchise fee percentage factor to revenues generated by transportation customers. Thus, as a replacement for franchise fees under Sections 6000-6302, we find no basis to conclude that receipt of municipal surcharges on DWR revenues would financially disadvantage the municipalities, as compared with franchise fees.

We therefore require the IOUs to continue to remit funds to the municipalities for DWR sales as prescribed in D.02-02-052, but clarify that such remittances are properly classified as municipal surcharges under the provisions of Code Sections 6352-6354.1, rather than "franchise fees" under Sections 6000-6302. To the extent there are administrative costs associated with having IOUs calculate, bill, collect and remit Municipal Surcharges, SCE states that such costs should not be significant and should be recoverable from DWR under the terms of SCE's Servicing Agreement with DWR. SCE does not see any impediments assuming that it is allowed to recover from its customers the municipal surcharges it remits on the DWR electric power.

III. Need for Further Legislative Remedies

A. Parties' Position

PG&E claims that legislation is necessary and appropriate to resolve this issue, and to ensure that cities and counties are not harmed by DWR's stepping into the shoes of the utilities to meet their net short positions. PG&E believes that in the interim until this issue is addressed by the Legislature, however, the Commission should not require the utilities to remit funds to cities and counties that is not due and owing under state franchise fee law.

SCE does not believe that legislation is necessary to resolve the franchise fee issue. SDG&E believes that one clarification of the law may be appropriate. In the event that a separate DWR bond charge line-item appears on the customers bill – not bundled with an energy charge line-item as is done today – the separate DWR bond charge line-item should be subject to the Municipal Surcharge. The charge is a financing cost of providing energy – *i.e.*, a charge that would reasonably be part of the commodity charge an ESP might impose on its customers. Under this reasoning, SDG&E explains, the bond charge would be added to the DWR commodity charge and form the basis for the Municipal Surcharge. SDG&E believes the responsibility for pursuing legislative clarification should fall to local government, if they believe it necessary, in cooperation with DWR and the utilities.

The Cities argue that if this Commission authorizes PG&E to collect franchise fees, the appropriate means to mount any challenge to the collection would be via appeal of the Commission's order, not a collateral attack via state court or elsewhere. Moreover, the Cities believe that any diminution of franchise fee payments due to this circumstance will almost certainly result in litigation

against the utilities on behalf of customers complaining of discriminatory rates and on behalf of municipalities.

B. Discussion

In view of the provision we adopt in this order for municipalities to be compensated for DWR sales based on the applicable municipal surcharge provisions as discussed above, we find no need to pursue further legislative action on this issue. If any municipality or other party believes that further legislative remedies are warranted or desirable to define or clarify the municipalities legal rights to compensation related to DWR sales under AB1X, they are free to pursue such actions as they deem appropriate.

IV. Ratemaking Considerations

A. Background

We next address the question of whether any further ratemaking or accounting measures need to be adopted in this order as a result of the instant order. In D.02-02-052, we authorized certain interim measures pending a final resolution of the dispute relating to franchise fees following analysis of the legal and factual issues involved.

We directed each IOU to continue remitting franchise fees to the municipalities related to the portion of gross receipts attributable to DWR power sales revenue and to establish a memorandum account to track franchise fee remittances associated with DWR sales. The memorandum account allows for segregation of DWR-related franchise fee remittances from other remittances, and provides appropriate record keeping for any subsequent ratemaking adjustments that might be warranted for shortfalls or surpluses in IOU cost recovery caused by variations in remittances.

We recognize that because municipal surcharges will be remitted as a percentage of DWR sales revenue, the portion of revenues collected from ratepayers that will be attributable to the municipal surcharge on DWR sales will fluctuate monthly. Since we did not change overall retail rate levels to reflect DWR costs at the time we adopted the DWR revenue requirement in D.02-02-052, there was likewise no change in the level of franchise fee remittances to municipalities.[10] We directed the IOUs to draw upon funds generated from then- existing rate levels as a basis to remit the franchise fees associated with DWR power sales.

B. Parties' Positions

SDG&E does not believe any further ratemaking or accounting measures are necessary in its case, but recommends that the Commission simply continue SDG&E's ratemaking treatment of franchise fees and municipal surcharges as previously implemented under D.01-09-059 and approved in D.01-10-035 (in which a provision for the recovery of franchise fees on DWR power sales was included.) This provision for franchise fees was reflected in the revised tariff sheets filed by SDG&E on September 27, 2001 in compliance with D.01-09-059. In response to D.01-09-059 SDG&E filed tariffs, customers taking power from DWR are billed the municipal surcharge (pursuant to Sections 6350 to 6354 of the Public Utilities Code) to compensate local government for the use of public lands. Under these tariffs, SDG&E states that it is already collecting the municipal surcharge for DWR sales and remitting those amounts to municipalities in accordance with D.01-05-059 and D.01-10-035 (which denied rehearing of D.01-09-059).

[10] Prior to the adoption of D.02-02-052, the IOUs had already been remitting franchise fees to the municipalities based on gross sales receipts, including sales by DWR.

SCE believes that the Commission should clarify what mechanism will be used for IOUs to be compensated for municipal surcharges remitted on power sold by DWR. SCE argues that the IOUs should not be required to subsidize municipal surcharges or bear any risk of undercollection of these costs. If the Commission does not authorize retail rates sufficient for SCE to recover franchise fees (or equivalent municipal surcharges) on power sold by DWR, SCE claims that DWR will be responsible for reimbursing SCE for those costs under Section 7.3(b) of the Servicing Agreement between DWR and SCE.

PG&E and SCE were authorized by the Commission to collect a surcharge on power delivered to its customers[11] that was intended to be used, in part, for payment of funds to DWR for power procured under AB1X. At the time the surcharge was authorized, the precise amount of the DWR revenue requirement had not yet been determined. Likewise, at the time that the DWR revenue requirement was implemented in D.02-02-052, we did not make specific findings on precisely what portion of the surcharge authorized in D.01-03-082 would be required to cover DWR remittances. Likewise, no specific findings have been made concerning whether the surcharge was intended to include franchise fees or municipal surcharges.

SCE states that the Commission has not considered how the collection of franchise fees (or municipal surcharges) might be affected by the requirement under D.02-02-052 that IOUs pay DWR a fixed amount for each kWh of power DWR supplies to IOU customers. SCE also states that the Commission has not

[11] PG&E and SCE were each authorized a 3 cents/kWh surcharge in D. 01-03-082 to provide funds to pay DWR-related obligations. The 3 cents/kWh surcharge took effect on June 3, 2001 pursuant to D.01-05-064.

clarified whether its previously authorized surcharges include, or should be "grossed-up" for, franchise fees or municipal surcharges.

PG&E did not offer specific comments concerning ratemaking considerations, but its position is that no funds should be remitted to municipalities under present statutory requirements.

C. Discussion

We conclude that previously authorized accounting and ratemaking measures adopted in D.02-02-052 adequately provide for the ongoing collection and remittance of municipal surcharges related to DWR revenues and that no additional measures need to be authorized for purposes of the instant order. To the extent that future rates may be adjusted to reflect variances between collections and remittances to municipalities, those adjustments can be considered as part of the overall review and revision of URG rate levels. On an ongoing monthly basis, any fluctuations in remittances of municipal surcharges can be accounted for through the memorandum accounts that have already been established for that purpose. These fluctuations can be taken into account in determining URG revenue needs through the same process as we described in D.02-02-052 with respect to remittances of charges to DWR. As we stated therein:

> "With fixed retail tariffed rates and a fixed per kWh charge payable to DWR, there is, in effect, an amount that the utility is entitled to receive for its own account for the kWh that it supplies to its retail customers. We will call this amount the "imputed utility rate." To the extent that the actual percentage of DWR sales to each utility's retail customers is either less than or exceeds the forecast percentage of DWR sales to those customers for any month, the customers' bills for that month will not reflect exactly the imputed utility rate for the kWh the utility

> provides. The balancing account mechanisms that we have authorized elsewhere in this order are intended to ensure that over time, the utility recovers its imputed utility rate by segregating the effects of DWR sales and providing for a true up of estimated to actual DWR sales and allocated costs." (*Mimeo.*, at 99.)

Since the municipal surcharges are remitted as a direct percentage of DWR revenues, the accounting and ratemaking procedures for the municipal surcharges logically should mirror the procedures previously established to segregate and true up URG revenues for variances in forecasted versus actual DWR sales. Accordingly, fluctuations in monthly remittances of municipal surcharges for DWR revenues will correspondingly affect the "imputed utility rate" reflected in the customer's bill for recovery of utility retained generation URG-related costs. Consistent with D.02-02-052, however, this order is not the appropriate place to determine or adopt specific retail rate adjustments in response to municipal surcharge fluctuations. The memorandum accounting records already being maintained by the IOUs provide a satisfactory vehicle for keeping track of actual collections and remittances, and for making any subsequent ratemaking adjustments that may be deemed appropriate.

To the extent that the funds collected under the surcharge previously authorized for PG&E and SCE in D.01-03-082 exceed remittances to DWR, any residual amount remains available to cover the municipal surcharges remitted relating to DWR sales. To the extent that remittances to DWR and remittances of municipal surcharges relating DWR sales revenues impact revenues collected by PG&E and SCE to recover URG costs, the Commission can address any necessary ratemaking adjustments as part of the overall review and revision of retail rates,

as discussed in D.02-02-052.[12] We reiterate our prohibition in D.02-02-052, however, on any double recovery of franchise fees on DWR sales from customers.

V. Comments on Draft Decision

The draft decision of Administrative Law Judge Thomas R. Pulsifer in this matter was mailed to the parties in accordance with Section 311(g)(1) and Rule 77.7 of the Rules of Practice and Procedure. Comments were filed on January 30, 2003, and reply comments were filed on February 4, 2003.

Comments on the draft decision were filed by PG&E, SCE, and the City and County of San Francisco and other municipalities ("CCSF"). SDG&E filed only reply comments. We have reviewed parties' comments and taken them into account in finalizing this order, as discussed below.

A. Comments of PG&E

PG&E asks the Commission to affirm that the amounts already remitted to cities and counties for franchise fee payments should not be recalculated based on the "municipal surcharges" approach. PG&E argues that the Commission should state this expressly to avoid confusion or disagreement between the utilities and the cities and counties. To the extent that previously submitted amounts were required to be recalculated, PG&E believes there is a possibility that additional payments to cities and counties would be necessary, or that refunds would have to be obtained from cities and counties during a period of very significant financial stress.

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[12] Any revision of retail rates for PG&E is subject to the Plan of Reorganization ultimately to be adopted for PG&E by U.S. Bankruptcy Court (Case No.01-30923 DM). Any revision of retail rates for SCE is subject to the terms of the Settlement Agreement entered into between SCE and the Commission on October 2, 2001.

PG&E also claims there is not enough information in the draft decision to allow the utilities to calculate the municipal surcharge associated with DWR power for a given municipality. PG&E identifies the components needed to make the calculation as (1) the amount of power provided by DWR to customers in each municipality, (2) the assumed cost of the power, and (3) the appropriate factor to be applied to the resulting revenues.[13] PG&E agrees that the third component is straightforward, and no modification is necessary to address that variable. However, PG&E believes that a method to estimate the amount delivered by DWR into each municipality is needed, as well as the amount that should be applied for the assumed cost of power.

PG&E recommends that the parties be allowed to provide additional input on these issues through a workshop, possibly followed by comments. The Commission would then address the approach to be used to estimate the amount of DWR power delivered into each municipality, and the assumed power cost that should be used, to calculate the municipal surcharge.

Neither SCE nor SDG&E support PG&E's proposal for a workshop. SCE states that because its billing system differs from that of PG&E, SCE does not share PG&E's problem as to how to calculate surcharge obligations to individual municipalities. SCE already knows the amount of DWR power each of its customers use and the DWR revenue associated with that usage.

SDG&E already has Commission-approved tariffs implementing the Municipal Surcharge, and is remitting those surcharge amounts to municipalities in accordance with D.01-09-059 and D.01-10-035 (which denied rehearing of

[13] *See,* Public Utilities Code Section 6353.

D.01-09-059). SDG&E, therefore, expresses no interest in, nor need for, a workshop, as proposed by PG&E.

The problems identified by PG&E in calculating the municipal surcharge associated with DWR power for a given municipality appear to be unique to PG&E's billing system, and no similar difficulty exists for SCE or SDG&E. Accordingly, SCE and SDG&E should not be required to participate in any workshop that relates to billing system issues unique to PG&E. Because of the limitations in PG&E's billing system, however, further steps will be required to produce sufficient delineation of DWR-related revenues for PG&E to determine the correct remittances to each municipality. We, therefore, grant PG&E's request for a workshop for this purpose, but excuse SCE and SDG&E from participating in it.

PG&E shall submit a proposed workshop agenda within 20 calendar days from the effective date of this order, to be filed and served on parties of record, identifying more specifically what technical issues need to be addressed through the workshop, as well as identifying the municipalities that should be notified concerning any workshop. We direct the staff of the Commission's Energy Division to coordinate with PG&E representatives, as warranted, to initiate further steps toward conducting a workshop and facilitating resolution of the billing system issues raised by PG&E.

PG&E also asks the Commission to confirm that any amounts it has already remitted to the municipalities should not be recalculated. We agree that where a utility has properly remitted municipal surcharge revenues to municipalities in accordance with applicable statutory provisions, there is no need to recalculate past remittances relating to DWR power as a result of this order. Yet, PG&E raises doubts as to whether any amounts it may have

previously remitted to municipalities based on DWR sales revenues represent the correct amounts due, since PG&E claims that it does not have enough information from the Commission to calculate the correct municipal surcharge remittance amount due to each municipality. Accordingly, it would be wrong for the Commission to state positively that no recalculations of PG&E's prior remittances shall be made, knowing that PG&E cannot presently verify if it has made the proper remittances for its past obligations to each municipality. Accordingly, we reserve judgment concerning the extent to which PG&E may need to recalculate the correct amounts of surcharge revenues related to past collections of DWR revenues pending the results of the workshop to be scheduled.

B. Comments of SCE

SCE asks that the Commission permit the IOUs to incorporate municipal surcharges associated with DWR's power purchases into its URG or generation revenue requirements in the event that the utility's total rate level is no longer frozen.

If utility rates are no longer frozen, SCE argues, no residual revenues will be available to cover such municipal surcharges. With the end of the rate freeze, SCE believes that revenue requirements and rate components are likely to be calculated in a "bottoms-up" manner. SCE thus proposes that the Commission address, as part of this order, the methodology for recovering municipal franchise fee surcharges upon the implementation of "bottoms-up" billing.

SDG&E disagrees with SCE on the need for the instant order to address recovery methodologies for municipal surcharges in anticipation of a time when "utility rates are no longer frozen." SDG&E argues that the Municipal Surcharge

is simply a line item on the bill that is the sole obligation of the customer to pay. Public Utilities Code Sections 6354 (c) and (d) specifically hold the utility harmless and allow the municipality to enforce the collection of the surcharge from the customer. Making the surcharge a component of a utility's revenue requirement would contravene the direct language and intent of the Legislature.

PG&E notes that the Commission has not addressed any generation-related or DWR power charge rate components for PG&E upon which to base bottoms-up billing. The Commission has stated that it will adopt generation- and procurement-related revenue requirements and rate components for PG&E in a later decision. Therefore, PG&E believes that the Commission should address the methodology for recovering municipal franchise fee surcharges under bottoms up billing at the same time that other related revenue requirement or billing methodologies are addressed.

We conclude that it is premature and beyond the scope of this order to adopt policies governing how, or to what extent, utility retail rate elements may warrant revision to reflect remittances of municipal surcharges associated with DWR revenues. At the time and in the proceeding where we take up the issue of adopting utility generation-related or DWR power charge retail rate components based on bottoms-up billing, we shall also address, as appropriate, the manner and extent of any adjustments for municipal surcharges associated with DWR revenues.

C. Comments of CCSF

CCSF claims that there is no basis in the record for the Draft Decision's finding that DWR revenues do not constitute receipts of the utilities. CCSF argues that this finding would require, at a minimum, an interpretation of specific franchise agreements between franchising parties, which is beyond the

jurisdiction of the Commission. Given that the Commission already has the authority to require collection of franchise fees, CCSF argues that the Commission should address this issue only if it later determines that municipal surcharges should be discontinued.

CCSF claims that the Commission should require collection of franchise fees rather than municipal surcharges on DWR supplied power, and that the Commission must ensure that franchise fees are remitted by the IOUs on revenues associated with power purchased by DWR for utility customers as well as on utility revenues.

We disagree with CCSF in claiming that there is no basis for finding that DWR revenues do not constitute receipts of the utilities. There is no need to examine specific terms of any franchise agreements to support this finding since we are relying on the provisions of the Water Code. The effect of Water Code Section 80110 is to make the utilities only billing and collection agents for delivery of power on behalf of DWR. Thus, pursuant to the Water Code, DWR's revenue requirement, although collected by the utilities, does not belong to the utilities. It is, therefore, proper to exclude DWR's revenues from the utilities' gross receipts for purposes of calculating franchise fee requirement. Otherwise, local governments could double recover the same revenue stream: once in having the utilities use it once in their own franchise fee calculation and then a second time in calculating the municipal franchise fee surcharge.

VI. Assignment of Proceeding

Loretta M. Lynch and Geoffrey F. Brown are the Assigned Commissioners and Thomas R. Pulsifer is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. Under the provisions of AB1X, the DWR took over responsibility for procuring and selling a portion of the electric power supplied to end use customers in the service territories of the three IOUs beginning in early 2001.

2. Because DWR retains title to the electric power that it has procured under Water Code Section 80110, and sold to end use customers, DWR sales revenue are not "receipts of the grantee" that form the basis for IOU remittances of franchise fees under Public Utilities Code Section 6006.

3. DWR has not included franchise fees as an element of its revenue requirement under AB1X, and has not remitted franchise fees to municipalities related to AB1X sales revenue.

4. Senate Bill 278 (1993) adopted the Municipal Lands Surcharge Act ("the Act" or "SB 278") which imposed a surcharge on gas and electric sales by entities other than the incumbent utility.

5. Public Utilities Code Section 6350 states that the intent of the municipal surcharge is "to replace, but not increase, franchise fees that would have been collected pursuant to this division if not for changes in the regulatory environment such as the 'unbundling' of the gas industry."

6. Public Utilities Code Section 6352 (a) states that "[n]otwithstanding any other provision of law, a transportation customer who receives transportation service on [an] electric transmission or distribution system . . . subject to a franchise agreement executed pursuant to this division from an energy transporter shall be subject to a surcharge as defined in Section 6353."

7. In response to D.01-09-059 SDG&E filed tariffs under which customers taking power from DWR are billed the municipal surcharge (pursuant to

Sections 6350 to 6354 of the Public Utilities Code) to compensate local government for the use of public lands.

8. Under its tariffs SDG&E is already collecting the municipal surcharge for DWR sales and remitting those amounts to municipalities in accordance with D.01-05-059 and D.01-10-035 (which denied rehearing of D.01-09-059).

9. PG&E's billing system does not produce a sufficiently detailed delineation to calculate the correct municipal surcharge remittance amount relating to DWR revenues due to each municipality.

10. Further steps will be required to produce sufficient delineation of DWR-related revenues for PG&E to determine the correct remittances to each municipality.

Conclusions of Law

1. The municipalities should not be deprived of receipts that would otherwise be realized merely because DWR took over procurement responsibility to meet the residual net short requirements of the IOUs pursuant to AB1X.

2. DWR revenues are not a component of the "receipts of the grantee" which form the basis for franchise fees under Public Utilities Code Section 6006. Title to the underlying electric power (and sales there from) is held by DWR, not the IOU.

3. End-use customers purchasing power from DWR are subject to the municipal surcharge created by SB 278 (1993) as refined by SB 703 (1997).

4. End-use customers that purchase power from DWR under AB1X are "transportation customers" under the provisions of the municipal charge.

5. Since the municipal surcharges to be remitted will be determined as a percentage of DWR revenues, the accounting procedures for the municipal surcharges should mirror the procedures previously established to segregate and

true up URG revenues as a result of fluctuations in DWR sales as a percentage of total sales to endues customers.

6. It is not necessary for new legislation to be initiated in order to resolve the dispute over franchise fees.

7. To the extent that remittances of charges to DWR and remittances of municipal surcharges to municipalities relating DWR sales revenues impact revenues available to recover URG costs, the Commission can address any necessary ratemaking adjustments for municipal surcharges in the same manner and under the same time frame as for remittances of DWR revenue requirement charges.

8. It is premature and beyond the scope of this order to adopt policies governing how, or to what extent, utility retail rate elements may warrant revision to reflect remittances of municipal surcharges associated with DWR revenues.

9. To the extent that a utility has properly remitted past municipal surcharge revenues to municipalities in accordance with applicable statutory provisions, there is no need to recalculate past remittance obligations relating to DWR power merely as a result of this order.

10. PG&E's request should be granted for a workshop addressing how the requisite data can be developed to facilitate the proper remittances of surcharges to municipalities.

11. Any determination of whether recalculation of PG&E's prior remittances to municipalities are necessary will be made after conclusion of the workshop, and the filing of a status report by PG&E as ordered below.

12. SCE and SDG&E should be excused from participating in the PG&E workshop since their billing systems already provide for proper calculation of municipal surcharge remittances.

O R D E R

IT IS ORDERED that:

1. Each of the investor-owned utilities (IOUs) shall bear responsibility for making remittances to municipalities for Department of Water Resources (DWR) revenues under the provisions of the municipal surcharge set forth in Public Utilities Code Sections 6350 *et. seq.*

2. Each IOU shall continue to maintain the memorandum accounts that were authorized in D.02-02-052 established for the purpose of tracking remittances made to municipalities relating to DWR revenues, and to account for any differences between proceeds collected and funds remitted for the municipal surcharges on DWR revenues, pending further notice and disposition by the Commission.

3. Further disposition of any differences between collections and remittances by each IOU for municipal surcharges for DWR revenues shall be addressed in a manner consistent with the Commission's ratemaking treatment of under/overcollections in utility retained generation URG revenues due to the effects of DWR revenue requirement remittances.

4. PG&E's request is hereby granted for a workshop to address how the requisite data can be developed to facilitate the proper remittances of surcharges to municipalities.

5. SCE and SDG&E are excused from participating in the PG&E workshop.

6. PG&E shall submit a proposed workshop agenda within 20 calendar days from the effective date of this order, to be filed and served on parties of record, identifying more specifically what technical issues need to be addressed through the workshop, as well as identifying the municipalities that should be notified concerning any workshop.

7. Upon conclusion of the workshop, PG&E shall promptly file and serve a written status report indicating the disposition of issues. The Commission's Energy Division will not be required to submit any workshop report.

This order is effective today.

Dated February 13, 2003, at San Francisco, California.

MICHAEL R. PEEVEY
President
CARL W. WOOD
LORETTA M. LYNCH
GEOFFREY F. BROWN
SUSAN P. KENNEDY
Commissioners